

**Improvements Are Needed to Comply With  
Legal and Procedural Requirements for  
Collection Statute Extensions and  
Installment Agreements**

**August 2001**

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DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

August 2, 2001

MEMORANDUM FOR COMMISSIONER, SMALL BUSINESS/SELF-EMPLOYED  
DIVISION  
COMMISSIONER, WAGE AND INVESTMENT DIVISION

A handwritten signature in cursive script, reading "Pamela J. Gardiner".

FROM: Pamela J. Gardiner  
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Improvements Are Needed to Comply With  
Legal and Procedural Requirements for Collection Statute  
Extensions and Installment Agreements

This report presents the results of our review and recommendations regarding collection statute extensions. The objective of this review was to determine if the Internal Revenue Service (IRS) was complying with the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> §§ 3461(a) and (c) and internal procedures involving extensions of the collection statute of limitations.

In summary, we found that the IRS secured some collection statute extensions without also securing the related installment agreement or levy release as required by law and internal procedures. In addition, many of the collection statute extensions secured with installment agreements involved extension dates that were not properly calculated. Further, the IRS does not have a comprehensive plan to identify, correct, and process the tax accounts that should have the collection statute expiration dates reduced to the later of the 10-year collection statute of limitations date or December 31, 2002. As a result, the IRS may not have sufficient time to complete its review of collection statute expiration dates and to take appropriate collection action.

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

We recommended that the IRS clarify procedures to ensure that collection statute extensions are approved concurrently with a related installment agreement or levy release and communicate the procedures to applicable employees and managers. Taxpayer accounts that we identified with collection statute expiration dates that are inaccurate or do not comply with the law should be reviewed and corrected. Nationally standardized procedures should be developed to centrally store collection statute forms within area offices. In addition, the IRS needs to develop a comprehensive plan for timely implementing the provisions of RRA 98 § 3461(c) and for taking actions to collect the remaining tax liabilities before the statutes expire.

IRS management agreed with these recommendations. However, management's response stated that the outcome of additional collection action on accounts that have a reduced collection statute expiration date may be limited because of the age of the accounts and the lack of collection options. We believe these accounts have the potential to be collected because they met the following criteria:

- The account case histories indicated that the accounts had never been classified as "Currently Not Collectible" by the IRS. (The IRS classifies accounts as "Currently Not Collectible" once the collection options have been exhausted.)
- The accounts met the IRS' criteria for taking enforcement action to collect delinquent liabilities. However, to receive the proper priority, the collection statute expiration dates must be corrected to show the reduced (i.e., earlier) statute expiration dates.

Management's comments have been incorporated into the report where appropriate, and the full text of their comments is included as an appendix.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions or Maurice S. Moody, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

# Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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### **Executive Summary**

The Internal Revenue Service (IRS) generally must collect federal tax, including penalties and interest, within 10 years of the date the tax was assessed. This 10-year period is referred to as the collection statute of limitations. Normally, the collection statute cannot be extended without the taxpayer's written agreement. The IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> § 3461(a) limits the use of collection statute extensions to allow them only in connection with an installment agreement or levy release. The reason for these exceptions is that a taxpayer may benefit from a release of a levy or from being able to pay the tax in installment payments past the original collection statute expiration date. In addition, RRA 98 § 3461(c) provides that collection statute extensions requested before the effective date of the law, January 1, 2000, that are not in connection with an installment agreement, will expire on the later of the 10-year collection statute of limitations date or December 31, 2002.

The overall objective of this audit was to determine if the IRS was complying with RRA 98 §§ 3461(a) and (c), as well as the Internal Revenue Code (I.R.C.), and internal procedures covering collection statute extensions obtained in connection with installment agreements before the effective date of the RRA 98.

### **Results**

The IRS was not fully complying with RRA 98 §§ 3461(a) and (c) and with internal procedures. For example, some of the collection statute extensions were secured without also securing the related installment agreement or levy release as required by law and internal procedures. In addition, the IRS does not have a comprehensive plan to adequately identify, correct, and process the tax accounts that should have the collection statute expiration date reduced to December 31, 2002. As a result, the IRS may not have sufficient time to complete its review of collection statute expiration dates and to take appropriate collection action.

Moreover, the IRS' review and approval processes for collection statute extensions and installment agreements were not adequate to ensure the computations were accurate and in compliance with laws and/or internal procedures.

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

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### **Collection Statute Extensions Were Sometimes Secured Without Also Securing the Related Installment Agreement or Levy Release As Required**

RRA 98 § 3461(a) limits the use of collection statute extensions to allow them only in connection with an installment agreement or levy release. This provision was effective for collection statute extensions requested after December 31, 1999. In addition, to help ensure that it would be compliant with the law, the IRS implemented its own procedures with this same requirement in August 1998.<sup>2</sup>

We reviewed collection statute extensions that were recorded between January 2 and April 1, 2000, for 968 taxpayers and determined that the IRS was not in compliance with RRA 98 § 3461(a) or its own procedures for 102 taxpayers (11 percent). For the 102 taxpayers, the collection statute extensions were secured without also securing the related installment agreement or levy release as required. In most of the cases in which the case history was available, it appeared that the IRS and the taxpayer intended to establish an installment agreement; however, the installment agreement was never processed or approved.

- In 16 cases (2 percent), the extensions were requested after December 31, 1999, the effective date of RRA 98 § 3461(a). The collection statute extensions for these cases may not be legally valid, increasing the risk that over \$153,000 in tax liabilities may not be collected.
- In 20 cases (2 percent), the case histories were not available to determine whether the date of the extension request was after December 31, 1999. As a result, we could not determine whether the requests were in compliance with RRA 98 § 3461. These extension requests were prohibited by IRS procedures and if it is determined that the extensions were requested after December 31, 1999, the statute extensions may not be legally valid.
- In 66 cases (7 percent), the extensions were requested before December 31, 1999. These were prohibited by IRS procedures that were effective in August 1998 but not by RRA 98 § 3461, since the requests were secured before the effective date of this provision.

Any collection activity performed after the original collection statute expiration date for the 16 extensions that may not be legally valid could violate these taxpayers' rights.

These improper extensions may have occurred because the IRS approving officials did not always review and approve the collection statute extension and the installment

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<sup>2</sup> Memorandum from Chief Operations Officer to District Directors, Service Center Directors, Regional Chief Compliance Officers, Regional Chiefs Customer Service and Assistant Commissioner (International), dated August 17, 1998.

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agreement at the same time to ensure that the statute extension was based on an installment agreement or levy release. IRS procedures do not require statute extension approval requests to be submitted simultaneously with the approval requests for installment agreements.

### **Actions to Evaluate and Update Collection Statute Expiration Dates May Not Be Completed in Time to Fully Comply With the Law**

RRA 98 § 3461(c) provides that collection statute extensions requested on or before December 31, 1999, that are not in connection with an installment agreement will expire on the later of the 10-year collection statute of limitations date or December 31, 2002. Although the IRS has identified some actions to implement this provision, it did not develop a comprehensive plan of action that considers all the appropriate issues. For example, to determine whether the collection statute extension was secured in connection with an installment agreement, the IRS plans to generate a report in October 2001 to provide a listing of accounts to be manually reviewed. To perform the manual review of these accounts, the IRS must obtain closed case histories. However, case histories may not be available or will be difficult to obtain depending on how long ago the collection statute extension was secured. In addition, the IRS has not determined the amount of resources that will be needed for the high volume of taxpayer accounts where the correct collection statute expiration date must be manually calculated.

Based on our analysis of the IRS' database, approximately 56,000 taxpayer accounts must be manually reviewed between January and June 2002. After the manual review, the IRS plans to run a computer program in July 2002 to review the accounts and systemically adjust the collection statute expiration date if the collection statute extension was not recorded within 4 weeks of an installment agreement. However, the IRS' criteria for the computer review may cause erroneous adjustments on taxpayer accounts for the following reasons:

- The manual review of accounts may not be properly performed or completed to ensure the accuracy of the collection statute expiration dates. For example, accounts that do not fall under the provisions of RRA 98 § 3461, such as those with special statute considerations, may have their statutes improperly shortened if the special considerations are not included in the calculations. Also, accounts that should have their statutes shortened may not be correctly identified by the computer program.
- There were 402 accounts in which the collection statute extension was requested in 1999 but recorded on the IRS' computer systems in 2000. The collection statute expiration dates should be reduced, but according to the IRS' criteria, these accounts would be excluded from both the manual and computer review.

The proposed dates for completion of the manual review may not provide enough time to properly review and correct all appropriate tax accounts. This may lead to incorrect

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collection statute expiration dates and insufficient time for the IRS to collect \$289 million that may be collectible before the statutes expire. The IRS will have less than 6 months to collect remaining tax liabilities for accounts on which the computer program changes the collection statute expiration date to December 31, 2002. However, the IRS generally does not assign cases for collection action less than 6 months before the collection statute expires, so any remaining liability on these accounts may not be collected.

If the statute dates for the 56,000 accounts are incorrectly revised as a result of the July 2002 computer program, it could result in incorrect records and inequitable treatment of taxpayers. This could affect management's ability to rely on the collection statute expiration date in the system and may lead to potential violations of taxpayers' rights.

The delays in implementing RRA 98 § 3461(c) as well as the limitations of the IRS' proposed methodology were caused by the lack of a comprehensive plan that factors in the appropriate time, availability of case documentation, and resources needed to determine the correct collection statute extension dates. If the IRS does not expedite the development of an adequate plan, it is at risk of not properly implementing this provision.

### **The Internal Revenue Service Could Not Provide the Documentation to Support Some of the Collection Statute Extensions Recorded on Its Computer Systems**

In order to extend the statute of limitations period for collection, the IRS must obtain from the taxpayer an executed Tax Collection Waiver (Form 900), which specifies the tax period and the statutory extension date. IRS administrative procedures also require an IRS official to approve and sign the agreement once it has been signed by the taxpayer. However, the IRS could not provide adequate documentation to support 233 of the 968 (24 percent) collection statute expiration dates that were recorded on the taxpayer accounts we reviewed. In most of these cases, the IRS could not locate the collection statute extension forms or provided the carbon copy part of the Form 900 that does not include the taxpayer's signature. In certain cases, the revised statute expiration date shown on the Form 900 was different from the date recorded on the taxpayer's account.

Without the necessary documentation, the IRS cannot support the collection statute extensions for 206 taxpayer accounts. Taxpayer rights may be violated if these statute extensions are not valid and if the IRS collects money on these accounts after the collection statute has already expired. For the 27 accounts in which the date on the Form 900 does not match the date recorded on the taxpayer's account, the risk is increased that at least \$352,000 may not be collected because the IRS is relying on an incorrect collection statute expiration date.

The inability of the IRS to locate the documents needed to support the collection statute extensions appears to be caused by outdated guidance on properly storing the Forms 900.

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In addition, the cases in which the date on the Form 900 was different from the date recorded on the taxpayer's account were due to errors made when the cases were input to the computer system.

### **Collection Statute Extensions and Installment Agreements Were Not Always Accurately Calculated for the Necessary Time and Payment Amount to Fully Satisfy the Tax Liability**

We reviewed 761 tax modules,<sup>3</sup> from 387 taxpayer accounts, to determine whether the collection statute extensions and installment agreements were computed to allow adequate time to fully pay the tax liability as required by IRS procedures and by law.<sup>4</sup> These 761 tax modules were covered by installment agreements and did not have penalty or interest restrictions; therefore, the time needed for the installment payments to fully pay the liability could be computed using the IRS computer system. Of the 761 tax modules, 625 (82 percent) had collection statute extensions and/or installment agreements that were not computed in accordance with the law or IRS procedures.

- The collection statute extension period was too short, by an average of 32 months, for 337 tax modules (44 percent). The collection statute would expire before the liability would be paid.
- The liability would never be paid for 33 tax modules (4 percent), regardless of the statute extension date, because the accruing interest is greater than the payments.
- The collection statute extension period was longer than needed, by an average of 37 months, to allow the installment payments to fully satisfy the tax liability for 255 tax modules (34 percent).

For the 370 tax modules (222 taxpayers) included in the first two bulleted items above, the taxpayers will have a remaining liability of \$1.8 million that the IRS will have to write off when the collection statutes expire. Further, for the 255 tax modules (154 taxpayer accounts) in which the collection statute expiration date was extended for too long a period, if any of these taxpayers default on their installment agreements, they would be subject to collection activity longer than if the collection statute expiration dates had been calculated according to the IRS' internal procedures.

Additionally, in our computer extract of accounts with collection statute expiration dates extended in the first quarter of Calendar Year 2000 (1,866 tax modules), 62 tax modules were extended more than 5 years (the maximum time allowed under IRS procedures) past the 10-year collection statute expiration date.

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<sup>3</sup> A tax module is the part of a taxpayer's account that includes information for one type of tax for one tax period. Collection statute extensions must be separately computed for each tax module.

<sup>4</sup> I.R.C. § 6159 (1988).

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The IRS' procedures indicate that its computer system should be used to assist in computing the amount of time required to fully satisfy a liability for each tax module, including accruals of penalties and interest, as long as the tax module does not have penalties and interest restrictions. However, employees were not always following the procedures. None of the 761 tax modules involved restrictions, so the IRS' system could have been used to systemically calculate the correct full payment date for each tax module. Moreover, the required documents are not always provided simultaneously to IRS managers so that they may properly review and approve collection statute extensions and the associated installment agreements. Without reviewing the computations for the full payment dates, managers do not have a basis for approving the collection statute extensions or installment agreements.

### **Summary of Recommendations**

We recommend that the Commissioners of the Small Business/Self-Employed (SB/SE) and the Wage and Investment (W&I) Divisions clarify procedures to ensure that collection statute extensions are approved concurrently with a related installment agreement or levy release. Procedures should also be updated based on the IRS reorganization to reflect the new locations for storing signed collection statute forms. SB/SE Division and W&I Division management should review the taxpayer accounts that we identified as inaccurate or that may not comply with the law and take appropriate action to correct the collection statute expiration dates. The IRS should develop a comprehensive plan for implementing the provisions of RRA 98 § 3461(c) and for taking actions to collect the remaining tax liabilities before the statutes expire.

Management's Response: The IRS Commissioner agreed with the recommendations in the report and plans to take appropriate corrective action. The corrective actions planned include training for IRS employees and managers on computing collection statute extension and installment agreement time periods, revising the conditions for approval of these documents, and updating the requirements for their storage. The IRS will also take additional actions to implement the provisions of RRA 98 § 3461(c) and develop a plan to address the collection potential from accounts with reduced collection statute expiration dates. Management's complete response to the draft report is included as Appendix V.

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## Objective and Scope

*The overall objective of this audit was to determine if the IRS is complying with RRA 98 §§ 3461 (a) and (c), as well as the I.R.C., and internal procedures covering collection statute extensions obtained in connection with installment agreements.*

The overall objective of this audit was to determine if the Internal Revenue Service (IRS) was complying with the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> §§ 3461 (a) and (c), as well as the Internal Revenue Code (I.R.C.), and internal procedures covering collection statute extensions obtained in connection with installment agreements.

The audit scope included all collection statute extension agreements that were input to the IRS' computer system from January 2 to April 1, 2000, and any related installment agreement. It also included an analysis of all taxpayer accounts in which a collection statute extension was still in effect and was input to the IRS' computer system before December 31, 1999. We interviewed National Headquarters personnel to obtain the information needed to evaluate the IRS' plans and procedures developed to implement the two RRA 98 § 3461 provisions. We also interviewed field employees in the former Los Angeles, Manhattan, Midwest, Southern California, and South Florida District Offices. The audit work was performed from February through December 2000. This audit was performed in accordance with *Government Auditing Standards*.

Details of our audit objective, scope, and methodology are presented in Appendix I. Major contributors to this report are listed in Appendix II.

## Background

The IRS generally must collect federal tax, including penalties and interest, within 10 years of the date the tax was assessed. This 10-year period is referred to as the

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

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collection statute of limitations. Normally, the collection statute cannot be extended without the taxpayer's written agreement.

Prior to the passage of the RRA 98, there were no restrictions on the IRS' ability to enter into a written agreement, or even multiple agreements, with a taxpayer to extend the 10-year statute of limitations for collection of tax. To address concerns that these extension agreements allowed the IRS to take collection enforcement action for too long a period, RRA 98 § 3461(a) amended I.R.C. § 6502(a) (Supp. IV 1998) to prohibit collection statute extension agreements after December 31, 1999, except in two specific situations:

- If the collection statute extension agreement is in connection with an agreement to pay the balance due in installment payments (known as an installment agreement).
- If the collection statute extension agreement involves the release of a levy.

The reason for these exceptions is that a taxpayer may benefit from a release of levy or from being able to pay the tax in installment payments past the original collection statute expiration date. The restrictions became effective for collection statute extension requests made after December 31, 1999.

Although RRA 98 § 3461(a) does not provide any limitation on the length of time the collection statute of limitations can be extended in connection with an installment agreement, IRS procedures (effective August 1998) prohibit extending a collection statute beyond 5 years after the original collection statute expiration date, even with an installment agreement.

*An agreement to extend the collection statute on or before December 31, 1999, without an installment agreement, will expire on the later of the 10-year statute of limitations date or December 31, 2002.*

RRA 98 § 3461(c) provides that an agreement to extend the collection statute that was requested on or before December 31, 1999, will expire on the later of the 10-year collection statute of limitations date or December 31, 2002, if not in connection with an installment agreement. To comply with this provision, the IRS must review accounts with extended collection

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statutes to determine whether the extensions were in connection with installment agreements.

### Results

*Some of the collection statute extensions reviewed were not in connection with an installment agreement or levy release.*

*The IRS does not have a comprehensive plan to process the tax accounts that should have a reduced collection statute expiration date.*

The IRS was not fully complying with RRA 98 §§ 3461(a) and (c) and with internal procedures. For example, some of the collection statute extensions were secured without also securing the related installment agreement or levy release, as required by law and internal procedures. In addition, the IRS does not have a comprehensive plan to adequately identify, correct, and process the tax accounts that should have the collection statute expiration date reduced to December 31, 2002. As a result, the IRS may not have sufficient time to complete its review of collection statute expiration dates and to take appropriate collection action.

For some of the accounts with extended collection statute expiration dates, the IRS was unable to provide copies of the collection statute extension, Tax Collection Waiver (Form 900), or provided the carbon copy part of the Form that does not have the taxpayer's signature. In other cases, the revised statute expiration date shown on the Form 900 was different from the date recorded on the taxpayer's account.

In addition, the IRS' review and approval process for determining the full payment date and revised collection statute expiration date was not always adequate to ensure the computations were accurate and in compliance with laws and/or internal procedures.

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### Collection Statute Extensions Were Sometimes Secured Without Also Securing the Related Installment Agreement or Levy Release As Required

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RRA 98 § 3461(a)<sup>2</sup> limits the use of collection statute extension requests to allow them only in connection with an installment agreement or levy release. This provision became effective for collection statute extensions requested after December 31, 1999. In addition, to help ensure that it would be compliant with the law, the IRS implemented its own procedures for this provision in August 1998.<sup>3</sup> To determine whether the IRS was in compliance with this RRA 98 provision and its own internal procedures, we obtained a computer extract of collection statute extensions that were input between January 2 and April 1, 2000, as well as the associated Forms 900. We analyzed the computer extract, Forms 900, and available case histories to determine the request date of the collection statute extension and to determine whether the extension was in connection with an installment agreement or levy release.

*Of the 968 accounts reviewed, 102 had collection statute extensions that were not secured in connection with an installment agreement or levy release.*

Of the 968 taxpayer accounts in which a collection statute extension was input between January 2 and April 1, 2000, the IRS was not in compliance with RRA 98 § 3461(a) or its own procedures for 102 taxpayers (11 percent). For the 102 taxpayers, the collection statute extensions were secured without also securing the related installment agreement or levy release as required. In most of the cases in which the case history was available, it appeared that the IRS and the taxpayer intended to establish an installment

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<sup>2</sup> This RRA 98 section amended I.R.C. § 6502(a)(2) and was effective for collection statute extension requests made after December 31, 1999.

<sup>3</sup> Memorandum from Chief Operations Officer to District Directors, Service Center Directors, Regional Chief Compliance Officers, Regional Chiefs Customer Service and Assistant Commissioner (International), dated August 17, 1998.

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agreement; however, the installment agreement was never processed or approved.

- In 16 cases (2 percent), the extensions were requested after December 31, 1999, the effective date of RRA 98 § 3461(a). The collection statute extensions for these taxpayers may not be legally valid, increasing the risk that over \$153,000 in tax liabilities may not be collected. If these extensions are not legally valid, the collection statute expiration date should be revised back to the prior collection statute expiration date. The potentially incorrect collection statute expiration dates on the IRS' computer system indicate to IRS employees that there is more time to collect than is actually allowed by law.
- In 20 cases (2 percent), the taxpayer case histories were not available to determine whether the date of the extension request was after December 31, 1999. As a result, we could not determine whether the requests were in compliance with RRA 98 § 3461. These extension requests were prohibited by the IRS' internal procedures because they were not secured in connection with an installment agreement or levy release. If the extensions were requested after December 31, 1999, the statute extensions may not be legally valid.
- In 66 cases (7 percent), the extensions were requested before December 31, 1999. These were prohibited by the IRS' internal procedures that became effective in August 1998 but were not prohibited by law, since the requests were secured before the effective date of RRA 98 § 3461.

*The rights of 16 taxpayers could be violated because a collection statute extension was not secured with an installment agreement or levy release after the effective date of the law.*

Any collection activity performed after the original collection statute expiration date for the extensions that may not be legally valid could violate the rights of 16 taxpayers. For example, if a collection statute extension was requested on January 23, 2000, to extend the collection statute expiration from the original date of April 15, 2004, to November 28, 2006, the extension would not be legally valid if it was not secured in

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connection with an installment agreement or levy release. Any attempt to collect the tax after April 15, 2004, would be a violation of the law and the taxpayer's rights.

For the 16 cases which may not be legally valid, the IRS discussed an installment agreement with the taxpayer, but it was not approved for the following reasons:

- It was determined that the taxpayers could not meet the original payment terms.
- The length of time on the collection statute extension was inadequate.
- The installment agreements were not sent for approval and input to the IRS' computer system.

These improper extensions may have occurred because the IRS approving officials did not always review and approve the collection statute extension and the installment agreement at the same time to ensure that the statute extension was based on an installment agreement. Based upon the case histories reviewed, none of the collection statute extensions involved a discussion of a levy release.

*The IRS' internal procedures do not require that the collection statute extensions and installment agreements receive approval at the same time.*

The IRS' internal procedures require managerial approval on both the installment agreement and the collection statute extension.<sup>4</sup> However, the procedures do not require submission of both the installment agreement and the collection statute extension for approval at the same time. Because of the requirements of RRA 98 § 3461(a), approval of the collection statute extension must be contingent on the approval of an installment agreement or levy release. Approval of the documents should take place once the signed and dated collection statute extension form is received back from the taxpayer. If IRS officials required collection statute extensions and installment agreements or levy releases to be reviewed and input to the IRS' computer system at the same time, it would better ensure that collection

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<sup>4</sup> Internal Revenue Manual (IRM) § 5.14 (October 18, 1999).

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statute extensions are approved only in connection with an installment agreement or levy release.

### Recommendations

The Commissioners of the Small Business/Self-Employed (SB/SE) and the Wage and Investment (W&I) Divisions should implement the following recommendations:

*Procedures should be issued to ensure that collection statute extensions are submitted for approval only with an installment agreement or levy release.*

1. Clarify procedures to require that approving officials approve both the installment agreement or levy release and the Form 900 simultaneously and ensure the revised collection statute expiration date is extended beyond the full payment date of the installment agreement.

Once the procedures are clarified, communicate them to the applicable IRS employees and managers to ensure they are aware of the changes.

Management's Response: The IRS plans to revise the IRM with new procedures that:

- Require the same manager to approve the installment agreement (or levy release) and Form 900 simultaneously.
  - Clearly emphasize that the revised collection statute expiration date must be after the full payment date of the installment agreement.
  - Provide a review process to ensure employees follow these new procedures.
2. Correct the collection statute expiration dates on the 16 taxpayer accounts in which an installment agreement was not secured with the Form 900 as required by RRA 98 § 3461(a).

Management's Response: The IRS will change the computer records for these accounts to reflect their true collection statute expiration dates.

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### **Actions to Evaluate and Update Collection Statute Expiration Dates May Not Be Completed in Time to Fully Comply With the Law**

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*RRA 98 § 3461(c) provides that collection statute extensions requested on or before December 31, 1999, that are not secured in connection with an installment agreement will expire on the later of the 10-year collection statute of limitations date or December 31, 2002.*

*Although the IRS has identified some actions to implement RRA 98 § 3461(c), it did not develop a comprehensive plan of action that considers all the appropriate issues to ensure collection statute expiration dates are correctly changed.*

RRA 98 § 3461(c) provides that collection statute extensions requested on or before December 31, 1999, that are not in connection with an installment agreement will expire on the later of the 10-year collection statute of limitations date or December 31, 2002.

To determine whether the IRS will be in compliance with this RRA provision, we discussed with IRS officials the proposed methodology for analyzing accounts and changing the collection statute expiration dates, as appropriate, to comply with the new legal requirements. We also analyzed a computer extract of all taxpayer accounts in which a collection statute extension was still in effect and was input to the IRS' computer system before December 31, 1999, to determine the volume of collection statute extensions that the IRS may need to review.

Although the IRS has identified some actions to implement RRA 98 § 3461(c), it did not develop a comprehensive plan of action that considers all the appropriate issues. In addition, the IRS has not determined the amount of resources necessary to review the high volume of accounts with collection statute extensions input before December 31, 1999, that would require a manual calculation of the collection statute expiration date.

The IRS plans to generate a report in October 2001 that will provide a listing of accounts to be manually reviewed. From January through June 2002, IRS employees will manually review these accounts to determine which ones do not meet the criteria to have the collection statute expiration dates changed. In July 2002, programming changes will be made to systemically change applicable accounts to the correct collection statute expiration dates (the later of the 10-year collection statute of limitations date or December 31, 2002).

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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The IRS plans to manually review all accounts that meet the following criteria:

- The collection statute extension was input before January 1, 2000.
- The collection statute was extended beyond December 31, 2002.
- The total liability on the taxpayer's account is greater than \$5,000.

*Based on our analysis of the IRS' database and the IRS criteria for cases it intends to manually review, approximately 56,000 taxpayer accounts must be manually reviewed within a 6-month period.*

The manual review of taxpayer accounts during this 6-month period may present significant problems for the IRS. Based on our analysis of the IRS' database using these criteria, approximately 56,000 taxpayer accounts must be manually reviewed during this time period. To conduct the required review, the IRS must obtain the taxpayer case histories to determine whether the collection statute extension was secured in connection with an installment agreement. However, case histories may not be available or will be difficult to obtain, depending on how long ago the collection statute extension was secured. Most of the cases subject to review would have been closed before January 1, 2000. Taxpayer case histories for closed collection field cases are retained for approximately 3 years, and automated case histories are limited to the most recent case actions because of space limitations.

In addition, some of these taxpayer accounts have other factors, such as bankruptcy, litigation, and pending Offers in Compromise, which affect the collection statute expiration date. These factors are considered special collection statute considerations because the collection statute expiration date is legally suspended for a period of time. These considerations require additional calculations to properly compute the collection statute expiration date. Of the 56,000 accounts to be reviewed, approximately 13,000 taxpayers have these special collection statute considerations.

Because of the potential problems in obtaining case histories and the large volume of accounts to review, it

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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will be difficult for the IRS to properly review and determine the correct collection statute expiration dates for all appropriate tax accounts by June 2002. For accounts in which IRS employees do not note that the collection statute expiration date on the account is already correct, the IRS' planned July 2002 computer program will systemically adjust the collection statute expiration date to the later of the 10-year collection statute of limitations date or December 31, 2002, if the collection statute extension was not recorded within 4 weeks of an installment agreement.

However, the IRS' criteria for the computer review may not result in a proper adjustment to the collection statute expiration date on taxpayer accounts for the following reasons:

- If the manual review of accounts is not properly performed or completed, the computer program may make erroneous adjustments to collection statute expiration dates. For example, accounts that do not fall under the provisions of RRA 98 § 3461, such as those with special statute considerations, may have their statutes improperly shortened if the special considerations are not included in the calculations. Also, accounts that should have their statutes shortened may not be correctly identified by the computer program. This would apply, for example, to accounts with collection statute extensions that were not secured in connection with an installment agreement but were input within 4 weeks of the installment agreement.
- The manual and computer review criteria did not include 402 accounts in which the collection statute extension was requested in 1999 but input in the IRS' computer system in 2000. The collection statute expiration dates should be reduced, but according to the IRS' criteria, these accounts would not be reviewed. We provided a list of these accounts to the SB/SE Division compliance

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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managers and they agreed to include these accounts in the manual review.

*Once the computer program changes the collection statute expiration date on appropriate taxpayer accounts to December 31, 2002, the IRS will have less than 6 months to collect the remaining tax liabilities.*

In addition, the late dates for the manual (January – June 2002) and computer reviews (July 2002) may not give the IRS adequate time in which to take collection action on the accounts before the expiration of the reduced collection statute expiration date. Once the computer program changes the collection statute expiration dates to December 31, 2002, on applicable taxpayer accounts, the IRS will have less than 6 months to collect the remaining tax liabilities. However, the IRS generally does not assign cases for collection action less than 6 months before the collection statute expires, so any remaining liability on these accounts may not be collected.

*Approximately 7,100 taxpayer accounts with \$289 million in liabilities may be collectible.*

Completing the update of the collection statute expiration dates timely will allow the IRS enough time to take appropriate collection action on these accounts. Of the 56,000 taxpayer accounts meeting the criteria for review, approximately 7,100 accounts with \$289 million in liabilities may be collectible. These cases meet the IRS' criteria for collection enforcement action, have collection statute extensions that were not recorded within 4 weeks of an installment agreement, and have not been classified by the IRS as "Currently Not Collectible."

Additionally, if the statute dates are incorrectly revised for any of the 56,000 accounts as a result of the July 2002 computer program, it could result in inequitable treatment of taxpayers and potential violations of taxpayers' rights.

The delays in implementing RRA 98 § 3461(c), as well as the limitations of the IRS' proposed methodology, were caused by the lack of a comprehensive plan that factors in the appropriate time, availability of case documentation, and resources needed to determine the correct collection statute extension dates. If the IRS does not expedite the development of an adequate plan, it is at risk of not properly implementing this RRA 98

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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provision and losing the revenue that could be obtained during the extended collection period.

### Recommendation

3. The Commissioners of the SB/SE and W&I Divisions should develop a comprehensive plan for implementing the provisions of RRA 98 § 3461(c). The plan should begin the analysis and account review as soon as possible so that conversion to appropriate collection statute extension dates can be completed with sufficient time in which to take appropriate collection action. Further, it should provide information on the resources that will be provided for this effort and guidance on the allocation of these resources, as well as the course of action to take if case histories are not available. A plan for collecting the tax liabilities on accounts with reduced collection statute extension dates should also be included.

Management's Response: The IRS plans to complete several actions to fully implement the provisions of RRA 98 § 3461(c), including:

- Providing instructions for case reviews.
- Developing a plan to address the collection potential from these accounts.
- Developing instructions for review teams to consider special statute circumstances so that collection statute expiration dates are not inappropriately shortened.
- Providing procedures for the handling and disposition of accounts - including instructions concerning the extent of collection efforts to be attempted.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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### **The Internal Revenue Service Could Not Provide the Documentation to Support Some of the Collection Statute Extensions Recorded on Its Computer Systems**

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*To extend a collection statute, the IRS must obtain a signed agreement from the taxpayer for the specific date to which the statute is extended.*

To extend the collection statute of limitations period, the IRS must obtain from the taxpayer an executed Form 900, which specifies the tax period and the statutory extension date. To further ensure that the agreement is adequate to cover the period of time needed to collect the tax, IRS administrative procedures also require an IRS official to approve and sign the agreement once it has been signed by the taxpayer. These requirements are intended to protect the taxpayers' as well as the government's interest if the collection statute expiration date is ever disputed.

*In many of the cases reviewed, the IRS could not locate the collection statute extension forms.*

However, the IRS could not provide adequate documentation to support 233 of the 968 (24 percent) collection statute expiration dates that were recorded on the taxpayer accounts we reviewed. In most of these cases, the IRS could not locate the collection statute extension forms or provided the carbon copy part of the Form 900 that does not include the taxpayer's signature. In other cases, the revised statute expiration date shown on the Form 900 was different from the date recorded on the taxpayer's account. The following table shows reasons why the collection statute extension was not supported by documentation.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

### Collection Statute Extensions That Were Not Supported by Documentation

Number of Taxpayer Accounts Extended	Reason Why the Collection Statute Extension Was Not Supported
194	The IRS could not provide the supporting Form 900.
12	The IRS provided the carbon copy part of the Form 900 that does not include the taxpayer's signature.
27	The extended date on the Form 900 was different from the date on the IRS' computer system.
233	<b>TOTAL</b>

Without the necessary documentation, the IRS cannot support the collection statute extensions for 206 (194 plus 12 noted in the table above) taxpayer accounts. Taxpayer rights may be violated if these statute extensions are not valid and if the IRS takes action to collect money on these accounts after the collection statute has expired.

*For the 27 taxpayer accounts in which the collection statute expiration date on the Form 900 does not match the date recorded on the taxpayer's account, at least \$352,000 is at risk of becoming uncollectible.*

For the 27 taxpayer accounts in which the collection statute expiration date on the Form 900 does not match the date recorded on the taxpayer's account, the risk is increased that at least \$352,000 may not be collected because the IRS is relying on an incorrect collection statute expiration date.

In addition to the 233 collection statute extensions that were not supported, there were 21 collection statute extensions that were not approved by an IRS official as required by IRS procedures. While these extensions may still be legally valid, the requirement for managerial approval is an important control to ensure that collection statute extensions comply with legal and procedural requirements.

*The IRS' inability to locate the documents supporting the collection statute extensions appears to be caused by outdated guidance.*

The IRS' inability to locate the documents needed to support the collection statute extensions appears to be caused by outdated guidance on properly storing the Forms 900 as a result of the IRS reorganization. Previous IRS procedures required a copy of the

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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Forms 900 to be stored at a central location within each district. However, because of organizational changes, these procedures are not being followed. For example, one Automated Collection System (ACS) site attempted to send the collection statute extensions to the district office as required by former procedures, but the district office sent them back because the ACS site was no longer considered a part of the district office. No new procedures have been developed for storing the Forms 900.

In addition, the outdated procedures did not specify which part of the Form 900 to store. Parts 1 through 3 of the Form have the taxpayer's and IRS manager's signatures, whereas part 4 does not. If the IRS does not properly retain copies of the signed documents, it has no assurance that taxpayers agreed to these collection statute extensions.

The cases that had a date on the Form 900 that was different from the date recorded on the taxpayer's account were a result of errors made during input to the IRS computer system.

### **Recommendations**

The Commissioners of the SB/SE and W&I Divisions should implement the following recommendations:

4. Update the IRM based on the IRS reorganization to reflect the new locations for storing signed collection statute extension forms in each of the new IRS business units.

Management's Response: The IRS plans to revise the IRM with new procedures that will address how waivers will be stored.

5. Discuss with the IRS Office of Chief Counsel whether the extensions are legally valid for the 206 taxpayer accounts in which the IRS either did not provide a copy of the Form 900 or could not determine if the Form had been properly signed.

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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Correct the taxpayers' accounts for any extensions that are determined not to be legally valid.

Management's Response: The IRS Chief Counsel advised that the IRS may rely on its computer records and other circumstantial evidence to show that the statute of limitations on collection was extended or suspended due to litigation, bankruptcy, offer in compromise, or by agreement with the taxpayer. Based on its Chief Counsel's advice, the IRS concluded the waivers are legally valid.

Office of Audit Comment: The missing documentation for these statute extensions still leaves the possibility that the dates in the computer are incorrect or that the taxpayers never formally agreed to the collection statute extensions. For example, we identified that the collection statute expiration dates recorded on the IRS computer system did not always match the dates on the Form 900 signed by the taxpayer.

6. Correct the 27 taxpayer accounts in which the extended date on the Form 900 does not match the date on the taxpayer's account as shown on the IRS' computer system.

Management's Response: The IRS will change the computer records for these accounts to reflect the proper collection statute expiration dates.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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### Collection Statute Extensions and Installment Agreements Were Not Always Accurately Calculated for the Necessary Time and Payment Amount to Fully Satisfy the Tax Liability

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*The IRS' internal procedures prescribe that the collection statute expiration date should be extended only long enough for the installment payments to satisfy the tax liability, plus approximately 3 months, and not longer than 5 years past the original collection statute expiration date.*

I.R.C. § 6159(a)<sup>5</sup> allows the IRS to enter into written agreements with any taxpayer under which the taxpayer is allowed to satisfy liability for payment of any tax in installment payments if the IRS determines that the agreement will facilitate collection of the liability. To ensure that the installment agreement facilitates the collection of the liability, the IRS must properly compute the payments and time needed to pay the liability. Once this is determined, if the time needed goes beyond the 10-year collection statute of limitations, the IRS may request the taxpayer to sign a collection statute extension. The IRS' internal procedures prescribe that the collection statute expiration date should be extended only long enough for the installment payments to satisfy the tax liability, plus approximately 3 months, and not longer than 5 years past the original collection statute expiration date.<sup>6</sup>

The internal procedures also explain the process for computing the correct installment agreement and collection statute extension period. If a tax return is filed timely, the tax is assessed on the due date of the return. If the tax return is later subject to an examination and additional tax is assessed, the collection statute expires 10 years from the date of the additional assessment. As a result, the collection statute expiration dates may not always be in the same sequence as the tax periods. The computation should begin with the oldest assessed tax and be completed with the most recently assessed tax. The following table shows an example of the sequence in which installment payments should be applied.

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<sup>5</sup> I.R.C. § 6159(a) (1999).

<sup>6</sup> IRM 5.14.1.7 (October 18, 1999).

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### Example: Installment Payment Sequence to Use in Calculating the Length of an Installment Agreement

Tax Period Ended	Assessment Date	Sequence in Which Installment Payments Should Be Applied
December 31, 1990	April 15, 1995	2
December 31, 1991	April 15, 1995	3
December 31, 1992	April 15, 1993	1

In this example, the 1992 period would have the oldest assessed tax and the earliest collection statute expiration date. The installment payments would be applied first to the period ending December 31, 1992. Once the 1992 period was fully satisfied, the installment payments would be applied to 1990 and finally to 1991.

The IRS' procedures indicate that its computer system should be used to assist in computing the amount of time required to fully satisfy a liability for each tax module, including accruals of penalties and interest, as long as the tax module does not have restrictions on the computation of penalties and interest. Accounts with these restrictions cannot be properly calculated systemically because of limitations or complicating factors, such as business losses that can be applied to previous tax periods.

However, when completing collection statute extensions in connection with installment agreements, IRS employees did not ensure that the collection statute expiration dates and the installment agreements complied with legal and/or procedural requirements. In a majority of the cases reviewed, the collection statute expiration date was extended too long or not long enough, compared to the terms of the installment agreement. In some cases, the collection statute was extended more than the 5 years allowed by IRS procedures.

For the 968 taxpayer accounts for which the collection statute expiration date was extended during the period of January 2 through April 1, 2000, we analyzed the associated 1,866 tax modules. Of these 1,866 tax

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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*Of the 761 tax modules reviewed, 625 (82 percent) had collection statute extensions and installment agreements that were not computed in accordance with the law or IRS procedures.*

modules, there were 761 (from 387 taxpayer accounts) in which there were no penalty and interest restrictions and the accounts were still on installment agreements that had never been defaulted due to missed payments. Therefore, the time needed for the installment payments to pay the liability in full could be computed using the IRS' computer system.

We reviewed the 761 tax modules to determine whether the collection statute extensions and installment agreements were correctly computed to allow the taxpayers adequate time in which to fully pay the tax liability, as required by law<sup>7</sup> and IRS procedures. Of the 761 tax modules, 625 (82 percent) had collection statute extensions and/or installment agreements that were not computed in accordance with the law or IRS procedures. The types of incorrect calculations we identified are as follows:

- The collection statute extension period was too short, by an average of 32 months, for 337 tax modules (44 percent). For these tax modules, the installment payments would not fully satisfy the tax liability by the end of the new statute extension period. For example, a tax module with an original collection statute expiration date of April 15, 2004, was extended to November 28, 2006, but the installment payments will not fully pay the tax liability until July 28, 2009.
- The liability would never be paid for 33 tax modules (4 percent), regardless of the statute extension date, because the accruing interest is greater than the payments. For example, an account with a balance due of \$1 million that has an installment agreement for \$100 per month would never be paid in full.
- The collection statute extension period was longer than needed, by an average of 37 months, to allow the installment payments to fully satisfy the tax liability for 255 tax modules (34 percent). For

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<sup>7</sup> I.R.C. § 6159 (1988).

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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example, a tax module has a collection statute expiration date of April 15, 2004, that was extended to November 28, 2006, but the tax will be paid in full on July 28, 2005. This is different from the IRS' internal procedures, which would have calculated the statute date as October 28, 2005.

*For the 370 tax modules, the IRS will have to write off a total of \$1.8 million when the collection statutes expire.*

For the 370 tax modules (222 taxpayers) noted in the first two bulleted items, the taxpayers will have a remaining liability of \$1.8 million that the IRS will have to write off when the collection statutes expire. Further, for the 255 tax modules (154 taxpayer accounts) in which the collection statute expiration date was extended for too long a period, if any of these taxpayers default on their installment agreements, they would be subject to collection activity longer than if the collection statute expiration dates had been calculated according to the IRS' internal procedures.

Additionally, in our computer extract of accounts with collection statute expiration dates extended in the first quarter of Calendar Year 2000 (1,866 tax modules), 62 tax modules were extended more than 5 years (the maximum time allowed under IRS procedures) past the 10-year collection statute expiration date.

The incorrectly calculated installment agreements and collection statute extensions occurred because IRS employees did not always follow internal procedures and requirements for computing the installment agreements and collection statute extension periods. Computations did not always begin with the oldest assessed tax and end with the most recently assessed tax. If the computations are not based on the timing of the assessments for each tax period, it can result in tax periods with collection statutes that expire before the tax is paid in full.

In addition, the case histories for some of the cases did not indicate whether the employee used the IRS' computer system to assist in making the correct computations to determine the number of payments and time required to fully satisfy the tax liability.

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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Further, the approval process is not functioning as intended because the required documents are not always provided to IRS managers concurrently so that they may properly review and approve the collection statute extensions and the associated installment agreements. Without reviewing the computations for the full payment dates, managers do not have a basis for approving the collection statute extensions or installment agreements.

### **Recommendation**

The approval process for installment agreements and collection statute extensions is addressed in Recommendation 1. In addition, the Commissioners of the SB/SE and W&I Divisions should implement the following recommendation:

7. Provide training to applicable IRS employees and managers on the requirements and the method to compute installment agreements and collection statute extensions, consistent with the law and IRS policy and procedures. The training should focus on the proper use of the IRS' newly revised computer system to make these computations.

Management's Response: The IRS plans to provide training to applicable employees and managers on the methods of computing installment agreements and collection statute extensions. The training will focus on the proper use of the IRS' newly revised computer system.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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### Conclusion

*The IRS should issue additional guidance to its employees and managers to promote compliance with the law and its own internal procedures governing collection statute extensions and installment agreements.*

In general, the IRS was not fully complying with RRA 98 §§ 3461(a) and (c) and internal procedures. Some of the collection statute extensions secured after the effective date of the law were secured without also securing the related installment agreement or levy release, as required by law and internal procedures. In addition, the IRS does not have a comprehensive plan to adequately identify, correct, and process the tax accounts that should have the collection statute expiration date reduced to the later of the 10-year collection statute of limitations date or December 31, 2002. As a result, the IRS may not have sufficient time to complete its review of collection statute expiration dates and take appropriate collection action. Further, the IRS' review and approval process of collection statute extensions and installment agreements was not adequate to ensure the computations were accurate and in compliance with laws and internal procedures.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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### Appendix I

#### Detailed Objective, Scope, and Methodology

The overall objective of this audit was to determine whether the Internal Revenue Service (IRS) was complying with the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> §§ 3461 (a) and (c), as well as the Internal Revenue Code (I.R.C.), and internal procedures covering collection statute extensions obtained in connection with installment agreements before the effective date of the RRA 98. To accomplish our objective, we performed the following tests:

- I. Determined whether the IRS is in compliance with RRA 98 § 3461(a), which prohibits extending the collection statute of limitations unless it is in connection with an installment agreement or levy release.
  - A. Obtained and analyzed an extract from the IRS' computer system that identified collection statute extensions posted from January 2 through April 1, 2000. There were collection statute extensions input on 1,866 tax modules for 968 taxpayers.
  - B. Attempted to obtain copies of the collection statute extension forms input to the IRS' computer system from January 2 through April 1, 2000, from all of the former district offices<sup>2</sup> and service centers. We requested the Tax Collection Waivers (Form 900) on 1,866 tax modules for 968 taxpayers and received Forms 900 for 1,520 tax modules for 788 taxpayers.<sup>3</sup>
  - C. Researched the IRS' installment agreement records for the extension forms requested in step I.B. to confirm whether extensions were related to an ongoing installment agreement.
    1. Determined if the extended date on the collection statute extension, Form 900, was properly calculated to last the length of the installment agreement plus 90 days, as required by the Internal Revenue Manual (IRM).

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

<sup>2</sup> The IRS district office structure that was in place at the time of this review has since been changed to a business unit structure.

<sup>3</sup> In the case of 14 taxpayers, we received Forms 900 but not for all extended tax modules. We received Forms 900 for all extended tax modules for 774 taxpayers.

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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2. For extensions that were not secured in connection with an installment agreement, researched the IRS' computer system to determine whether the collection statute extension was related to a levy release under I.R.C. § 6343.
  3. Reviewed available case histories to determine when the collection statute extensions were requested for extensions that were not secured in connection with an installment agreement or levy release. For those cases in which case histories were not available, the requests were not considered to be in connection with an installment agreement if there was no indication of an installment agreement on the taxpayer's account by February 6, 2001 (this date is approximately 10 months after the collection statute extension date was entered on the taxpayer's account).
  4. Determined if the extended date on the Form 900 was more than 5 years past the original 10-year collection statute expiration date.
  5. Determined if the taxpayer and an IRS approving official signed the Form 900.
  6. Determined if the extended date on the Form 900 matched the date on the IRS' computer system.
- II. Determined whether IRS managers and employees responsible for establishing collection statute extensions have been trained on RRA 98 §§ 3461(a) and (c).
- A. Reviewed nationally distributed RRA 98 §§ 3461(a) and (c) training material.
  - B. Reviewed national memoranda related to collection statute extension procedures.
  - C. Reviewed the IRM sections related to collection statute extensions and installment agreements.
  - D. Interviewed special procedures staff in the former IRS Collection Division in National Headquarters and in a judgmental sample of five field locations to determine their understanding of the RRA 98 provisions and the training provided for RRA 98 § 3461 and to obtain copies of internal correspondence. We also discussed problems and concerns with implementing this provision.
- III. Determined whether the IRS had implemented or had formulated an adequate plan to implement RRA 98 § 3461(c), which provides that collection statute extensions requested before the effective date of the law, January 1, 2000, that are not secured in connection with an installment agreement must be changed to the later of the 10-year collection statute of limitations date or December 31, 2002.

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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- A. Reviewed the law and procedures in the RRA 98, the I.R.C., and the IRM related to the collection statute updates required by the RRA 98.
- B. Interviewed IRS officials from the Information Systems Division and the former Collection Division who were responsible for the collection statute updates required by RRA 98 § 3461(c) and obtained information regarding the IRS' action plan and requests for information systems changes to update taxpayer accounts.
- C. Obtained and analyzed an extract from the IRS' computer system for business and individual accounts which identified collection statute changes (including extensions) posted on or before December 31, 1999, with a collection statute expiration date beyond December 31, 2002, and a balance due. These data were extracted on May 26, 2000, and included interest and penalty accrued up to that date.
  - 1. Determined the number of accounts that need to be reviewed by the IRS in order to determine the correct collection statute expiration date.
  - 2. Determined the number of accounts that may have special collection statute considerations, such as bankruptcy, litigation, and Offers in Compromise, that will affect the calculation of the correct collection statute expiration date.
  - 3. Determined the number of accounts and liabilities that the IRS still considers to be collectible. (Note: we considered accounts to be collectible if they met the IRS' criteria for collection enforcement action, had collection statute extensions that were not recorded within 4 weeks of an installment agreement, and had not been classified by the IRS as "Currently Not Collectible".)

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**Appendix II**

**Major Contributors to This Report**

Maurice S. Moody, Assistant Inspector General for Audit (Headquarters Operations and Exempt Organizations Programs)

Nancy A. Nakamura, Director

Michael E. McKenney, Audit Manager

Cheryl Cerqua, Senior Auditor

Thomas F. Polsfoot, Senior Auditor

Daniel M. Quinn, Senior Auditor

Joseph P. Smith, Senior Auditor

Cindy L. Wright, Auditor

James E. Adkisson, Computer Specialist

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**Appendix III**

**Report Distribution List**

Commissioner N:C  
Deputy Commissioner N:DC  
Chief Counsel CC  
Director, Compliance, Small Business/Self-Employed Division S:C  
Director, Compliance, Wage and Investment Division W:CP  
Director, Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis N:ADC:R:O  
Director, Tax Administration Coordination N:ADC:T  
National Taxpayer Advocate TA  
Office of Management Controls N:CFO:F:M

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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### Appendix IV

#### Outcome Measures

This appendix presents detailed information on the measurable impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

##### Type and Value of Outcome Measure:

- Taxpayer Rights – Potential; 16 taxpayer accounts with collection statute extensions that are potential violations of the law (see page 4).
- Revenue Protection – Potential; \$153,000 in tax liabilities that may not be collected due to potentially incorrect statute expiration dates on the Internal Revenue Service's (IRS) computer system for the 16 taxpayer accounts that were potential violations of the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> § 3461(a) (see page 4).

##### Methodology Used to Measure the Reported Benefit:

Using an extract from the IRS' computer system, we identified and reviewed collection statute extension agreements input to the IRS' computer between January 2 and April 1, 2000. There were a total of 968 taxpayers; 102 had a collection statute extension input to their accounts without an associated installment agreement.

The 16 taxpayers who had collection statute extensions that were potential violations of RRA 98 3461(a) had \$153,000 in outstanding liabilities as of November 24, 2000, that is at risk of not being collected if the IRS continues to rely on the incorrect collection statute expiration date. This amount is at risk because the IRS employees working the cases would not be aware of the correct collection statute expiration date and could base the timing of collection actions on incorrect information. For example, an installment agreement could be granted to a taxpayer based on the incorrect collection statute extension date. However, once the correct collection statute expiration date passed, the IRS would be prohibited by law from requiring any remaining installment payments.

##### Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$289 million in liabilities that may be collectible (see page 8).

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685 (codified as amended in scattered sections of 2 U.S.C., 5 U.S.C., 5 U.S.C. app., 16 U.S.C., 19 U.S.C., 22 U.S.C., 23 U.S.C., 26 U.S.C., 31 U.S.C., 38 U.S.C., and 49 U.S.C.).

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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- Taxpayer Rights – Potential; 56,000 taxpayer accounts that may be reviewed and changed (see page 8).

### Methodology Used to Measure the Reported Benefit:

From the IRS' computer system, we obtained an extract of every collection statute extension that was related to Tax Collection Waivers (Form 900) input prior to December 31, 1999. From this extract, we identified 56,000 taxpayer accounts that would need to be manually reviewed using the IRS' criteria. We also reviewed the IRS' plans for reviewing and correcting the collection statute expiration dates on these accounts and determined that the IRS' methodology could result in erroneous adjustments to the collection statute expiration dates because accounts that do not fall under the provisions of RRA 98 § 3461, such as those with special statute considerations, may have their statutes improperly shortened. In addition, accounts that should have their statutes shortened may not be correctly identified by the computer program.

From the same 56,000 taxpayer accounts, we identified 7,100 accounts totaling \$289 million in tax, penalties, and interest that may be collectible if collection action is expedited based upon the updated collection statute expiration date. These accounts met the IRS' criteria for collection enforcement action (not accounts in the queue) which did not have an installment agreement posted to the account within 4 weeks of the date the collection statute extension was input and had never been classified as "Currently Not Collectible."

### Type and Value of Outcome Measure:

- Taxpayer Rights – Potential; 206 taxpayer accounts that did not have proper documentation to support the collection statute expiration date recorded on the IRS' computer systems (see page 13).
- Revenue Protection – Potential; \$352,000 in taxes that may not be collected for 27 taxpayer accounts that did not have the correct collection statute expiration dates on the IRS' computer system (see page 13).

### Methodology Used to Measure the Reported Benefit:

Based on the extract from the IRS' computer system which contained collection statute extension agreements input to the computer system between January 2 and April 1, 2000, we requested copies of the Form 900 for 968 taxpayers. The IRS could not provide a Form 900 for 194 taxpayers, and 12 of the Forms 900 received were the carbon copy part of the Form that did not have the taxpayer's signature. In addition, 27 taxpayers' Form 900 had an "extended to" date different from the collection statute expiration date on the IRS' computer system.

The 27 taxpayers who had a collection statute extension date on the IRS' computer system that did not match the date shown on the Form 900 had \$352,000 in outstanding

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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liabilities as of October 30, 2000, that is at risk of not being collected if the IRS continues to rely on the incorrect collection statute expiration date. The risk is increased because the IRS employees working the cases would not be aware of the correct collection statute expiration date and could base the timing of collection actions on incorrect information.

### Type and Value of Outcome Measure:

- Revenue Protection – Potential; \$1.8 million that may be written off because the collection statute expiration date is not long enough for the taxpayer's installment payments to satisfy the liability or the accruing interest is greater than the taxpayers' computed payments (see page 17).
- Taxpayer Burden – Potential; 154 taxpayers with collection statute expiration dates that were extended longer than allowed by IRS procedures. If any of these taxpayers default on their installment agreements, they would be subject to collection activity longer than if the collection statute expiration dates had been calculated according to the IRS' internal procedures (see page 17).

### Methodology Used to Measure the Reported Benefit:

For the 968 taxpayer accounts for which the collection statute expiration date was extended during the period of January 2 through April 1, 2000, we analyzed the associated 1,866 tax modules. We recalculated, via the IRS' computer program, the collection statute dates for 761 tax modules in which there were no penalty and interest restrictions and the accounts were still on installment agreements that had never been defaulted due to missed payments. Of the 761 tax modules, 625 were not computed accurately. Of these, 255 tax modules (154 taxpayers) have collection statute extensions that were longer than allowed by the IRS' internal procedures.

For 370 of the 625 tax modules, the collection statute expiration date will expire prior to full payment of the balance due, which may require the IRS to write off \$1.8 million in liabilities.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

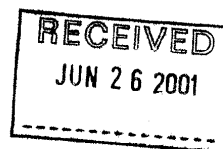
Appendix V

### Management's Response to the Draft Report



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

June 22, 2001



MEMORANDUM FOR DEPUTY INSPECTOR GENERAL FOR AUDIT

FROM:

*for* Charles O. Rossotti *Bob Wilensky*  
Commissioner of Internal Revenue

SUBJECT:

Draft Audit Report- Improvements Are Needed to Comply With  
Legal and Procedural Requirements for Collection Statute  
Extensions and Installment Agreements

We have made and will continue to make improvements to ensure we protect taxpayers rights and comply with the legal and procedural requirements for collection statute extensions and installment agreements.

We appreciate your recognition of our responsiveness to Section 3461(a) of RRA 98, which requires Revenue Officers to secure waivers of the Collection Statute Extension Date (CSED) only with installment agreements or levy releases. Your report acknowledges that, prior to the effective date of the law, our procedures limited use of CSED extensions to those secured in connection with installment agreements. In addition, to ensure appropriate use of these extensions, we established a policy whereby we only accept agreements that satisfy taxes within five years of the original CSED. You also acknowledge this in your report.

In 1999 we began identifying those accounts that would expire by law on December 31, 2002, both by programming requests and examination of accounts assigned to revenue officers.

Thank you for the opportunity to respond to your draft report on our compliance with Section 3461 of the Restructuring and Reform Act of 1998 (RRA 98) and our policies regarding CSED extensions.

As part of the IRS's overall strategic plan to provide better customer service, we recognize we need to further emphasize our current installment agreement procedures. In this response I address the actions we will take in accordance with your recommendations.

#### IDENTITY OF RECOMMENDATION 1

Clarify procedures to require that approving officials approve both the installment agreement or levy release and the Form 900 simultaneously and ensure the revised collection statute expiration date is extended beyond the full payment date of the

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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installment agreement. Once the procedures are clarified, communicate them to the applicable IRS employees and managers to ensure they are aware of the changes.

### **ASSESSMENT OF CAUSE**

Revenue Officers sometimes secured collection statute extensions without also securing the related installment agreement or levy release.

### **CORRECTIVE ACTION**

We will revise the Internal Revenue Manual (IRM) with new procedures that:

- Require the same manager to approve the installment agreement (or levy release) and Form 900 simultaneously
- Clearly emphasize the revised collection statute expiration date must be after the full payment date of the installment agreement
- Provide a review process to ensure employees follow these new procedures

### **IMPLEMENTATION DATE**

December 1, 2001

### **RESPONSIBLE OFFICIAL**

Director, Filing and Payment Compliance, Small Business/Self-Employed

### **CORRECTIVE ACTION MONITORING PLAN**

The appropriate functional staff will advise the Director, Filing and Payment Compliance of any delay in completing the corrective action.

### **IDENTITY OF RECOMMENDATION 2**

Correct the collection statute expiration dates on the 16 taxpayer accounts in which an installment agreement was not secured with the Form 900 as required by RRA 98 § 3461(a).

### **ASSESSMENT OF CAUSE**

Installment Agreements were not secured, as required, after the waiver was secured for the 16 accounts.

### **CORRECTIVE ACTION**

We will change the computer records for these accounts to reflect their true Collection Statute Expiration Dates (CSEDs).

### **IMPLEMENTATION DATE**

September 1, 2001

### **RESPONSIBLE OFFICIALS**

Director, Filing and Payment Compliance, Small Business/Self-Employed

### **CORRECTIVE ACTION MONITORING PLAN**

The appropriate functional staff will advise the Director, Filing and Payment Compliance of any delay in completing the corrective action.

## Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements

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### IDENTITY OF RECOMMENDATION 3

The Commissioners of the SB/SE and W&I Divisions should develop a comprehensive plan for implementing the provisions of RRA 98 § 3461(c). The plan should begin the analysis and account review as soon as possible so that conversion to appropriate collection statute extension dates can be completed with sufficient time in which to take appropriate collection action. Further, it should provide information on the resources that will be provided for this effort and guidance on the allocation of these resources, as well as the course of action to take if case histories are not available. A plan for collecting the tax liabilities on accounts with reduced collection statute extension dates should also be included.

### ASSESSMENT OF CAUSE

While work has progressed on the elements needed to implement RRA 98 § 3461(c), we have no overall action plan incorporating these activities set forth as a master document.

### CORRECTIVE ACTION

We have completed a number of actions to implement the provisions of RRA 98 Section 3461(c).

- By memorandum dated November 16, 2000, we asked Revenue Officers to review all cases in active inventory for subject CSEDs.
- We took preliminary steps beginning in 1999 to include a Request for Information Services (RISs) that provided systemic review and update of subject CSEDs; certain cases will require manual review due to lack of a systemic fix.
- We submitted a RIS to produce extracts of cases requiring manual review. Information Systems (IS) has accepted our RIS. We will provide the result of the extract run to the field in January, 2002.
- We submitted a RIS providing the programming to truncate statutes. IS accepted our RIS in 1999.

We need to complete several actions to fully implement the provisions of the section.

- We will solicit subject matter experts from the advisory, case processing, and service center functions to help us develop instructions for case reviews. (July 31, 2001)
- Management will develop a plan to address the collection potential from this population of accounts; the majority of the accounts have already been the subject of unsuccessful collection attempts. Many are already classified as currently not collectible (CNC). We will pursue these cases for additional collection will be based upon:
  - The anticipated return from the aged account relative to overall work priorities and resource availability
  - The current account status (e.g. active inventory, queue, CNC)
  - An established dollar criterion. (August 31, 2001)
- We will develop instructions for review teams that identify appropriate truncation cases, ensure that special statute circumstances (such as suspension in bankruptcy or offer in compromise) are not inappropriately truncated, and provide procedures for

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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the disposition/handling of accounts; instructions will reflect management decisions concerning the extent of collection efforts to be attempted. (October 01, 2001)

- We will conduct review of identified cases by teams beginning in early 2002; beginning dates are contingent upon receipt of account listings.
- We will complete case reviews (June, 2002)

### **IMPLEMENTATION DATE**

We will fully implement the corrective action as outlined above by July 1, 2002.

### **RESPONSIBLE OFFICIALS**

Director, Filing and Payment Compliance, Small Business/Self-Employed

### **CORRECTIVE ACTION MONITORING PLAN**

The appropriate functional staff will inform the Director, Filing and Payment Compliance of any delay in completing the corrective action.

### **IDENTITY OF RECOMMENDATION 4**

Update the IRM based on the IRS reorganization to reflect the new locations for storing signed collection statute extension forms in each of the new IRS business units.

### **ASSESSMENT OF CAUSE**

We did not update guidance on the storage of signed extension forms after the reorganization.

### **CORRECTIVE ACTION**

As noted in response to recommendation 1 above, we will include new procedures for processing waivers in the Internal Revenue Manual by December 31, 2001. We will include procedures and direction for employees, managers, review functions in this revision of the manual. The revision will also address how we will store waivers. The IRM revision will provide information on which copy of the waiver to use for input and which to store. The new procedures will resolve the problem identified by TIGTA on storage of the part of the form that contains the approving official's signature.

### **IMPLEMENTATION DATE**

January 1, 2002

### **RESPONSIBLE OFFICIALS**

Director, Filing and Payment Compliance, Small Business/Self-Employed

### **CORRECTIVE ACTION MONITORING PLAN**

The appropriate functional staff will advise the Director, Filing and Payment Compliance of any delay in completing the corrective action.

### **IDENTITY OF RECOMMENDATION 5**

Discuss with the IRS Office of Chief Counsel whether the extensions are legally valid for the 206 taxpayer accounts in which the IRS either did not provide a copy of the Form

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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900 or could not determine if the Form had been properly signed. Correct the taxpayers' accounts for any extensions that are determined not to be legally valid.

### **ASSESSMENT OF CAUSE**

The Service relied on its computerized records for the 206 accounts; paper copies were not always available.

### **CORRECTIVE ACTION**

During the audit, we discussed "whether the extensions are legally valid for the 206 taxpayer accounts in which the IRS either did not provide a copy of the Form 900 or could not determine if the Form had been properly signed," with our Chief Counsel. From this, and a prior opinion from Counsel, we concluded the waivers are legally valid.

According to Chief Counsel, "the Service may rely on its computerized records and other circumstantial evidence to show that the statute of limitations on collection was extended or suspended due to litigation, bankruptcy, offer in compromise, or by agreement with the taxpayer."

### **IMPLEMENTATION DATE**

Completed

### **RESPONSIBLE OFFICIAL**

Director, Filing and Payment Compliance, Small Business/Self-Employed

### **CORRECTIVE ACTION MONITORING PLAN**

N/A

### **IDENTITY OF RECOMMENDATION 6**

Correct the 27 taxpayer accounts in which the extended date on the Form 900 does not match the date on the taxpayer's account as shown on the IRS' computer system.

### **ASSESSMENT OF CAUSE**

We did not correctly record extension dates on the taxpayer's account due to input error.

### **CORRECTIVE ACTION**

We will revise the 27 taxpayer accounts to reflect the proper Collection Statute Expiration Dates (CSEDs).

### **IMPLEMENTATION DATE**

September 1, 2001

### **RESPONSIBLE OFFICIAL**

Director, Filing and Payment Compliance, Small Business/Self-Employed

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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### **CORRECTIVE ACTION MONITORING PLAN**

The appropriate functional staff will inform the Director, Filing and Payment Compliance of any delay in completing the corrective action.

### **IDENTITY OF RECOMMENDATION 7**

Provide training to applicable IRS employees and managers on the requirements and the method to compute installment agreements and collection statute extensions, consistent with the law and IRS policy and procedures. The training should focus on the proper use of the IRS' newly revised computer system to make these computations

### **ASSESSMENT OF CAUSE**

IRS employees were not always computing installment agreement and collection statute extensions correctly.

### **CORRECTIVE ACTION**

We will provide training consistent with the law and IRS policy and procedures to applicable IRS employees and managers on the requirements and the method to compute installment agreements and collection statute extensions. The training will focus on the proper use of the IRS' newly revised computer system to make these computations. We are also considering a policy change for the length of CSED extensions. The training program will be implemented as follows.

- Revise the Service policy on the length of CSED, as appropriate by December 1, 2001.
- Ensure the revised computer programming to enhance CSED computations is accurate by January 1, 2002.
- Develop a training module for CSED computations by February 1, 2002.
- Roll out training beginning June 1, 2002.

### **IMPLEMENTATION DATE**

We will complete all phases of the training program by September 1, 2002.

### **RESPONSIBLE OFFICIALS**

Director, Filing and Payment Compliance, Small Business/Self-Employed

### **CORRECTIVE ACTION MONITORING PLAN**

The appropriate functional staff will inform the Director, Filing and Payment Compliance of any delay in completing the corrective action.

### **OUTCOME MEASURES RESPONSE**

We understand how you reached your conclusions about the potential yield of updating the identified collection statute expiration dates. You based your conclusions, however, on assumptions of account collectibility, which are unconfirmed by the report's methodology. In a universe of aged accounts, the revenue potential of a case may be limited because of the lack of collection options. These issues may have been explored

## **Improvements Are Needed to Comply With Legal and Procedural Requirements for Collection Statute Extensions and Installment Agreements**

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earlier in the case life cycle. We will address these cases as outlined in our response to recommendation three.

Please call Martha Sullivan, Deputy Director, Compliance Policy, Small Business/Self-Employed, at (202) 622-5563 if you have any questions.